

The Star Biz

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By TEE LIN SAY

WELL, the Ninth Malaysian Plan (9MP) has finally been unveiled. It is perhaps time for the local bourse to catch its breath after weeks of excitement and rounds of speculation. For investors who might have missed out on the speculative plays; there is life after the 9MP. Its time to gather the dust and go back to basics: Invest in fundamental stocks.

Offering a rather compelling story, both on prospects and valuations, is low profile automated materials handling manufacturer Malaysian AE Models Holdings Bhd (Maemode).

Most analysts have been oblivious to the small waves this company has been making, in its effort to transform itself to a regional automated manufacturer. Still waters however, run deep.

Maemode is no longer a company that has cyclical earnings with heavy dependence on one-off projects. For one, expect recurring income to the tune of RM70mil – RM75mil over the next 10 years, mainly for maintenance and services from its current projects.

Maemode's group managing director and chairman Datuk Jimmy Lim Kee Sinn expects this recurring income to grow at 6%-8% as the group secures more high end projects.

"Maemode is moving up the value chain by eyeing mainly high end projects and is no longer competing with small manufacturing shops. Not only are margins better, but bigger projects also require servicing and maintenance work. This would mean recurring income for the company," says Lim.



Lim

For analysts concerned over its unsustainable revenue, Maemode seems to have addressed that worry. Since January this year, the low profile company has secured an additional RM80mil worth of contracts.

This brings its total orderbook to RM240mil, which will keep it busy over the next 12 months. Still, this is not to say that Maemode will need to scramble for new jobs once its current orderbook has been exhausted.

"Its current contract includes maintenance and technical jobs that provide an average annual recurring income of approximately RM70mil per annum for a duration of at least 10 years which reinforces the long term commitment of its customers," says SJ Securities research head Wee Kim Hong.

The Catalyst

The biggest catalyst for this company would perhaps be its latest joint venture (JV) company set up in Singapore to venture into the growing industry of conveyor systems, namely in coal mining.

For the record, Maemode has successfully secured a few projects in this industry in the last two years by outbidding some major international players.

Based on the joint venture agreement, Maemode will act as the project manager and will supply new automated systems to the coal mine in Balikpapan, Indonesia.

On an annual basis, Maemode expects the contribution from this industry alone to be in the range of RM70mil -RM75mil per year over the next ten years as coal will become a cheaper substitution for oil in the energy related industries.

Profit margins are also anticipated to rise to 9%. The recurring income from service and maintenance will be quite substantial as the estimated total length of the conveyor systems in Balikpapan is in the range of 30-35km.

“Before we constructed our conveyor systems, the coal mine needed thousands of lorries just to carry their coal everyday. With the completion of the first phase, the usage of the lorries has reduced drastically. This savings in logistic cost brings better margins for the coal mine operator,” says Lim.



The coalmine inloading system conveyor system in Balikpapan, Indonesia, constructed by Maemode.

And if earnings are anything to go by, this JV could be the next reason for a re-rating. For its first year of operations in Balikpapan, Maemode had constructed a conveyor belt measuring 2.8 km in length valued at RM28mil - RM30mil. This would translate into RM2.6mil -RM2.7mil in net profit.

Thus, for its current financial year (FY) ending May 2006, analysts are already anticipating better results. In FY05, Maemode recorded net profit of RM8.9mil on the back of RM186.04mil.

SJ's Wee is keeping his FY06 earnings forecast of 12.4 sen for the year ending May 2006. Wee is forecasting full year FY06 net profit of RM11.82mil, while Kenanga Research head of retail is forecasting RM11.2mil.

“Maemode should have no problem achieving those numbers as its third quarter for FY06 is likely to be better than the entire FY05,” says Wee.

Wee has a price target of RM2.15 based on prospective earnings per share for FY07 of 17.9 sen, pegging a PE of 12 times.

Kenanga Research head of retail Teoh Cheng Guan is equally as bullish. He has forecasted net profit of RM11.4mil and RM17.5mil for FY07 and FY08.

“Buy with a 12-month target price of RM1.90 based on a 3-year (FY05-FY08) price earnings growth ratio of 0.6x,” says Teoh.

Lim further indicates of an improved dividend policy due to stronger performance amounting to a payout ratio of about 12% and 16% for FY06 and FY07. Investors can perhaps expect dividends of 1.5 sen for FY06 and 3 sen in FY07.

As at Nov 31, 2005, Maemode has a net tangible asset of RM1.52 per share against its share price of RM1.

Diversified earnings base

Meanwhile, Maemode is not solely dependant on Malaysia for contracts, as it has substantial contracts in Canada, China, Indonesia, Japan and the United States among others. In Malaysia alone, it has approximately 700 customers, which would include OYL Industries Bhd and Panasonic Malaysia Sdn Bhd.

China is now the main earnings driver for the group, contributing approximately 35% of revenue. Maemode is not dependant on any single customer as the top 10 customers only account for approximately 28% of group sales and the biggest customer accounts for less than 6% of group sales.

Better margins in the coming financial years can also be attributed to lower group effective tax rate as three of Maemode's key subsidiaries will enjoy 5 to 10 year tax exemption under its pioneer status beginning June 2006.

For the uninitiated, Maemode has four core businesses. The unit materials handling systems contributes 18% to turnover, while the bulk materials handling systems contributes 24%. The logistic, sortation and warehousing systems contribute 26% while contract equipment manufacturing contributes 20%.

Conveyor systems are now widely used in factories of different industries. It is used in airports, warehouses, ports, construction sites and just about any industry that requires automated transfer.

On a macro outlook, the conveyer belt systems industry is experiencing a strong growth in the region. More and more companies are beginning to realise the efficiency and cost savings in having automated systems connect their goods straight from the jetty to their factories.

“In areas like Balikpapan Indonesia, where there is no proper infrastructure system in place, it would only make sense to have a conveyor belt. Lorries would cost even more, especially with higher fuel prices,” says Lim.

While Maemode does not have a direct competitor in its class within Malaysia, the closest comparison would be Singapore listed Inter Rollers Engineering Ltd, which is presently trading at

a PE of 18x. Inter Roller's share price has been surging sharply on the back of 'buy' recommendations and strong growth prospects.

Maemode is listed on the main board with a paid up capital of RM95mil. A notable shareholder would be British-based Atlantis Investment Management Ltd with a 12.56% stake.

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